Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:ITA:B03
PLR-106397-16
PLR-106398-16

Date:
August 23, 2016

TY:

LEGEND:

Acquirer Taxpayer =
Target Taxpayer =
Acquirer Sub =
Services =

Firm 1 =
Firm 2 =
Person A =
Person B =
Person C =
Person D =
Accounting Firm X =
Accounting Firm Y =
Year 1 =
Date 1 =
Date 2 =
Date 3 =
A =
B =
C =
D =
E =
F =
G =
H =
I =
J =
K =

L =

Dear :

This is in response to your letter dated February 25, 2016 sent by your representatives. In the letter, your representatives requested an extension of time to file the forms necessary to make a safe harbor election under Rev. Proc. 2011-29 to allocate success-based fees between facilitative and non-facilitative amounts incurred for a covered transaction for Acquirer Taxpayer's tax year ending Date 2 and for Target Taxpayer's short tax year ending Date 1. The request is based on sections 301.9100-1 and 301.9100-3 of the Procedure and Administrative Regulations.

FACTS

Target Taxpayer provides Services. On Date 1, Acquirer Taxpayer, through its wholly owned subsidiary Acquirer Sub, acquired 100 percent of the outstanding shares of Target Taxpayer's common stock. Following the transaction Target Taxpayer became a wholly owned subsidiary of Acquirer Sub and an indirect subsidiary of Acquirer Taxpayer. The total consideration was approximately $A million.

Target Taxpayer engaged Firm 1 to provide various services with respect to the transaction. Pursuant to the terms of the engagement letter, Firm 1 agreed to provide investment banking services regarding the possible acquisition of some or all of Target Taxpayer's business. The engagement letter provided that Firm 1 would be paid a transaction fee of B percent of the transaction value upon the closing date of a transaction. Prior to the completion of the transaction, Firm 1 sent a letter to Target Taxpayer to the effect that, if the acquisition was completed, Firm 1 would be paid a success-based fee of $C, in accordance with the engagement letter. Target Taxpayer represented that on Date 1, it provided Acquirer Taxpayer with $C from debt it took on as part of the transaction, and Acquirer Taxpayer paid the $C to Firm 1 by wire transfer upon closing of the transaction.

Also in conjunction with the transaction, Acquirer Taxpayer engaged Firm 2 to provide consulting services associated with the transaction. These services included advice, analysis, and assistance with respect to due diligence and other investigatory matters related to Target Taxpayer, its subsidiaries, and its parent companies in conjunction with the acquisition. Acquirer Taxpayer represented that it paid a total $D, of which $E was for services to secure financing (and thus not an amount qualifying as a success-based fee). Moreover, Acquirer Taxpayer also engaged two individuals, Person A and Person B, who provided consulting services, including due diligence and transaction structuring. Acquirer Taxpayer represented that it paid each of Person A and Person B $F. The total success-based fees for Firm 2, Person A and Person B were $G, payment of which was contingent upon the successful closing of the

transaction. Acquirer Taxpayer represented that it used funds transferred from Target Taxpayer to make these payments.

Target Taxpayer had engaged Accounting Firm X for preparation of its federal tax return for several years prior to the year in which the transaction occurred. Pursuant to this engagement, Accounting Firm X prepared a Form 1120, *U.S. Corporation Income Tax Return*, for a taxable year ending Date 2 on behalf of Target Taxpayer, a period which included the acquisition transaction. On the Form 1120 with a Date 2 year-end, Accounting Firm X allocated the $C success-based fee paid to Firm 1 as permitted under the safe-harbor election provided by Rev. Proc. 2011-29. Thus, that Form 1120 reflected that 70 percent of the fee, or $H, was deducted, and 30 percent, or $I, was capitalized. However, Accounting Firm X inadvertently did not include the election statement required under Rev. Proc. 2011-29 to properly make the election.

Accounting Firm X also included the success-based fees paid to Firm 2, Person A and Person B on Target Taxpayer's Form 1120 with a Date 2 year-end. Those fees were also allocated as permitted under Rev. Proc. 2011-29. However, Accounting Firm X determined that the success-based fees were start-up costs under section 195, and amortizable over 180 months. The amount deducted was $J, with the remaining $K to be deducted over the remaining months of the amortization period.

The Form 1120 with a Date 2 year-end was presented to Person C, Executive Vice President and Chief Financial Officer for Acquirer Taxpayer and Target Taxpayer; and to Person D, formerly Controller, Treasurer, and Chief Accounting Officer for Target Taxpayer. Person C delegated the detailed review and signature to Person D, who had been responsible for signing Target Taxpayer's tax returns in prior years and did so again with respect to the Date 2 year-end return. At all times, Person C believed the Form 1120 included a valid election under Rev. Proc. 2011-29 for the total amount of success-based fees.

Target Taxpayer's Form 1120 with a Date 2 year-end was timely filed. No return was filed for Acquirer Taxpayer for the tax year ending Date 2. Subsequent to the filing of Target Taxpayer's Form 1120 with a Date 2 year-end, Target Taxpayer entered into an engagement with Accounting Firm Y for the audit of its financial statements, as well as for tax compliance and advisory services. During the course of performing the audit of the Date 3 financial statements, Accounting Firm Y reviewed Target Taxpayer's Form 1120 with a Date 2 year-end. While doing so, Accounting Firm Y discovered that the election statement required to make the safe-harbor election for success-based fees was not included with that Form 1120, despite the fees being properly allocated as permitted by Rev. Proc 2011-29. During the course of discussions with Accounting Firm X and Accounting Firm Y, Person C determined that the best course of action would be to request relief for an extension of time to file the elections under Rev. Proc. 2011-29 pursuant to the authority of Treas. Reg. §§ 301.9100-1 and -3.

The Internal Revenue Service is examining Target Taxpayer's Date 2 year-end return and Acquirer Taxpayer's Date 3 year-end return. In conjunction with the examinations, it was determined that Target Taxpayer's Form 1120 filed with a tax year ending Date 2 should instead have reflected that it was a short-period return ending on the date the transaction closed, Date 1. It was also determined that the success-based fees for Acquirer Taxpayer should have been reported on a return for the tax year ending on Date 2 (which it did not file), not on Target Taxpayer's return.

LAW AND ANALYSIS

Section 263(a)(1) of the Internal Revenue Code and section 1.263(a)-2(a) of the Income Tax Regulations provide that no deduction shall be allowed for any amount paid out for property having a useful life substantially beyond the taxable year. In the case of an acquisition or reorganization of a business entity, costs that are incurred in the process of acquisition and that produce significant long-term benefits must be capitalized. INDOPCO, Inc. v. Commissioner, 503 U.S. 79, 89-90 (1992); Woodward v. Commissioner, 397 U.S. 572, 575-576 (1970).

Under section 1.263(a)-5, a taxpayer must capitalize an amount paid to facilitate a business acquisition or reorganization transaction described in section 1.263(a)-5(a). An amount is paid to facilitate a transaction described in section 1.263(a)-5(a) if the amount is paid in the process of investigating or otherwise pursuing the transaction.

Section 1.263(a)-5(f) of the Regulations provides that an amount that is contingent on the successful closing of a transaction described in section 1.263(a)-5(a), or success-based fee, is presumed to facilitate the transaction. A taxpayer may rebut the presumption by maintaining sufficient documentation to establish that a portion of the fee is allocable to activities that do not facilitate the transaction.

To reduce controversy between the IRS and taxpayers over the documentation required to allocate success-based fees alternatively to the regulatory presumption, the IRS issued Rev. Proc. 2011-29, 2011-1 C.B. 746. The revenue procedure states that the IRS would not challenge a taxpayer's allocation of a success-based fee between activities that facilitate a transaction described in section 1.263(a)-5(e)(3) and activities that do not facilitate the transaction if the taxpayer --

(1) treats 70 percent of the amount of the success-based fee as an amount that does not facilitate the transaction;

(2) capitalizes the remaining 30 percent as an amount that does facilitate the transaction; and

(3) attaches a statement to its original federal income tax return for the taxable year the success-based fee is paid or incurred, stating that the taxpayer is electing the safe

harbor, identifying the transaction, and stating the success-based fee amounts that are deducted and capitalized.

The revenue procedure applies to covered transactions described in section 1.263(a)-5(e)(3), which include --

(i) A taxable acquisition by the taxpayer of assets that constitute a trade or business;

(ii) A taxable acquisition of an ownership interest in a business entity (whether the taxpayer is the acquirer in the acquisition or the target of the acquisition) if, immediately after the acquisition, the acquirer and the target are related within the meaning of section 267(b) or section 707(b); or

(iii) A reorganization described in section 368(a)(1)(A), (B), or (C) or a reorganization described in section 368(a)(1)(D) in which stock or securities of the corporation to which the assets are transferred are distributed in a transaction which qualifies under section 354 or 356 (whether the taxpayer is the acquirer or the target in the reorganization).

Sections 301.9100-1 through 301.9100-3 of the Procedure and Administration Regulations provide the standards the Commissioner uses to determine whether to grant an extension of time to make a regulatory election. Section 301.9100-2 provides automatic extensions of time for making certain elections. Section 301.9100-3 provides extensions of time for making elections that do not meet the requirements of section 301.9100-2.

Section 301.9100-1(b) defines the term “regulatory election” as an election whose due date is prescribed by a regulation published in the Federal Register, or a revenue ruling, procedure, notice or announcement published in the Internal Revenue Bulletin.

Section 301.9100-1(c) provides that the Commissioner may grant a reasonable extension of time to make a regulatory election, or a statutory election (but no more than six months except in the case of a taxpayer who is abroad) under all subtitles of the Internal Revenue Code except subtitles E, G, H and I.

Section 301.9100-3 provides extensions of time to make a regulatory election under Code sections other than those for which section 301.9100-2 expressly permits automatic extensions. Requests for extensions of time for regulatory elections will be granted when the taxpayer provides evidence (including affidavits described in the regulations) to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government.

Section 301.9100-3(b)(1) states that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer --

(i) requests relief before the failure to make the regulatory election is discovered by the Service;

(ii) failed to make the election because of intervening events beyond the taxpayer's control;

(iii) failed to make the election because, after exercising due diligence, the taxpayer was unaware of the necessity for the election;

(iv) reasonably relied on the written advice of the Service; or

(v) reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make the election.

Under section 301.9100-3(b)(3), a taxpayer will not be considered to have acted reasonably and in good faith if the taxpayer --

(i) seeks to alter a return position for which an accuracy related penalty has been or could be imposed under section 6662 at the time the taxpayer requests relief (taking into account section 1.6664-2(c)(3)) and the new position requires or permits a regulatory election for which relief is requested;

(ii) was informed in all material respects of the required election and related tax consequences, but chose not to file the election; or

(iii) uses hindsight in requesting relief. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

Target Taxpayer and Acquirer Taxpayer in this case have represented that they have requested relief before the failure to make the regulatory election was discovered by the Service. Target Taxpayer and Acquirer Taxpayer has also represented that they reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise Target Taxpayer and Acquirer Taxpayer to make the election. Thus, under sections 301.9100-3(b)(1)(i) and 301.9100-3(b)(1)(v), Target Taxpayer and Acquirer Taxpayer will be deemed to have acted reasonably and in good faith. Target Taxpayer and Acquirer Taxpayer have also represented that none of the circumstances listed in section 301.9100-3(b)(3) apply.

Section 301.9100-3(c)(1)(i) provides, in part, that the interests of the government are prejudiced if granting relief would result in the taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money).

Similarly, if the tax consequences of more than one taxpayer are affected by the election, the Government's interests are prejudiced if extending the time for making the election may result in the affected taxpayers, in the aggregate, having a lower tax liability than if the election had been timely made. Section 301.9100-3(c)(1)(ii) provides, in part, that the interests of the government are ordinarily prejudiced if the taxable year in which the regulatory election should have been made, or any taxable years that would have been affected by the election had it been timely made, are closed by the period of limitations on assessment under section 6501(a) before the taxpayer's receipt of a ruling granting relief.

Under these criteria, the interests of the government are not prejudiced in this case. Target Taxpayer and Acquirer Taxpayer have represented that granting relief would not result in a lower tax liability in the aggregate for either taxpayer for all taxable years affected by the election than each taxpayer would have had if the election had been timely made (taking into account the time value of money). Target Taxpayer and Acquirer Taxpayer have also represented that granting relief would not result in a lower tax liability in the aggregate for both taxpayers than if the election had been timely made. Furthermore, the taxable years in which the regulatory election should have been made and any taxable years that would have been affected had it been timely made are not closed by the period of assessment.

CONCLUSION

Target Taxpayer's and Acquirer Taxpayer's elections are regulatory elections, as defined under section 301.9100-1(b), because the due date of the election is prescribed in Rev. Proc. 2011-29. In the present situation, the requirements of sections 301.9100-1, 301.9100-3(b)(1)(i), and 301.9100-3(b)(1)(v) of the regulations have been satisfied. The information and representations made by Target Taxpayer and Acquirer Taxpayer establish that they both acted reasonably and in good faith. Furthermore, granting an extension will not prejudice the interests of the Government. Target Taxpayer and Acquirer Taxpayer represented that each will not have a lower tax liability in the aggregate for all taxable years affected by the election if given permission to make the election than they would have if the election were made by the original deadline for making the election. Target Taxpayer also represented that the period of assessment for the short tax year ending Date 1 will not be closed before receipt of a ruling. Acquirer Taxpayer represented that the period of assessment for the tax year ending Date 2 will not be closed before receipt of a ruling. Accordingly, Target Taxpayer is granted an extension of time to file the statements required by section 4.01(3) of Rev. Proc. 2011-29 until 60 days following the date of this letter. Acquirer Taxpayer is granted an extension of time to file the statements required by section 4.01(3) of Rev. Proc. 2011-29 until the later of 60 days following the date of this letter or until 60 days after Office of the Associate Chief Counsel, Corporate grants Acquirer Taxpayer relief under sections 301.9100-1 and 301.9100-3 of the Procedure and Administrative Regulations to file a consolidated return for the tax year ending Date 2.

No opinion is expressed in this letter as to whether it is appropriate for Acquirer Taxpayer to file a consolidated tax return, whether Target Taxpayer may file an amended return for the tax year ending Date 1, or the tax treatment of the $C transferred by Target Taxpayer to Acquirer Taxpayer.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal income tax consequences of any aspect of any transaction or item discussed or referenced in this ruling including whether Target Taxpayer or Acquirer Taxpayer properly included the correct costs as its success-based fees subject to the election, or whether the transaction was within the scope of Rev. Proc. 2011-29.

This ruling is directed only to the taxpayers requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Christopher F. Kane
Chief, Branch 3
(Income Tax & Accounting)

cc: